

CALIFORNIA FRANCHISE TAX BOARD

Legal Ruling No. 029

June 25, 1958

CORPORATIONS: CHANGE FROM COMMERCIAL TO EXEMPT STATUS

Syllabus:

A corporation is subject to franchise tax only for that portion of the year prior to its qualification as an exempt corporation.

Taxpayer, a corporation, operated a hospital for profit and paid the franchise tax. In the middle of its taxable year it amended its articles and changed its operations to a non-profit basis thus qualifying as an exempt corporation. Advice is requested whether taxpayer's tax for the year of the change-over should be computed on a prorated basis.

In Bank of Alameda County v Mccolgan, 69 CA 2d, 464 the court described the franchise tax as a tax imposed on a corporation "for the privilege of exercising its corporate franchise. The tax may not be imposed upon a corporation still in existence which no longer enjoys the privilege of exercising such franchises; that is, the privilege of doing business for the purpose of gain or profit. The court went on to rule that a corporation which has given up this privilege in the middle of a taxable year should not be held liable for a full year's tax.

When a corporation forsakes the purpose of profit and undertakes a non-profit purpose, by the accepted means of amending its articles with the Secretary of State, it has effectively given up the privilege to which the franchise tax attaches. Thereafter it cannot be subjected to the tax. As a result, proration of the tax is necessitated where the surrender of the privilege is made in the middle of a taxable year, just as it is where a corporation surrenders its privilege by dissolution or withdrawal.